

Independent auditors' report to the shareholders of The Saudi British Bank (A Saudi Joint Stock Company)

Report on the audit of the consolidated financial statements

Opinion

We have audited the consolidated financial statements of The Saudi British Bank ("SABB" or the "Bank") and its subsidiaries (collectively referred to as the "Group"), which comprise the consolidated statement of financial position as at 31 December 2017, and the consolidated statement of income, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and the summary of significant accounting policies and other explanatory notes from 1 to 41.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2017, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS") as modified by the Saudi Arabian Monetary Authority ("SAMA") for the accounting of zakat and income tax.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing as endorsed in the Kingdom of Saudi Arabia. Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Consolidated Financial Statements section of our report. We are independent of the Group in accordance with the professional code of conduct and ethics as endorsed in the Kingdom of Saudi Arabia, that are relevant to our audit of the consolidated financial statements, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, a description of how our audit addressed the matter is provided in that context:

Independent auditors' report to the shareholders of The Saudi British Bank (A Saudi Joint Stock Company)

Report on the audit of the consolidated financial statements (continued)

Key audit matters (continued)

Key audit matter	How our audit addressed the key audit matter
<p><i>Impairment of loans and advances</i></p> <p>As at 31 December 2017, the gross loans and advances was Saudi Riyals 120.562 billion against which impairment provision of Saudi Riyals 3.556 billion was maintained. This includes impairment against specific financing and collective impairment recorded on a portfolio basis through modelling.</p> <p>We considered this as a key audit matter as the Group makes complex and subjective judgements and makes assumptions to determine the impairment and the timing of recognition of such impairment.</p> <p>In particular, the determination of impairment against loans and advances includes:</p> <ul style="list-style-type: none"> ○ The identification of impairment events and judgments used to calculate the impairment against specific corporate loans and advances; ○ The use of assumptions underlying the calculation of collective impairment for portfolios of loans and advances, and the use of the models to make those calculations; and ○ An assessment of the Group's exposure to certain economic sectors affected by current economic conditions. <p><i>Refer to note 2(m) to the consolidated financial statements for the significant accounting policy relating to impairment of loans and advances, note 6 which details the disclosure of impairment against loans and advances and note 1.1(f)(i) which explains the impairment assessment methodology used by the Group.</i></p>	<p>We assessed the design and implementation, and tested the operating effectiveness of the key controls over management's processes for establishing and monitoring both specific and collective impairment. This included testing of:</p> <ul style="list-style-type: none"> - entity level controls over the modelling process including model review, and monitoring and approval of assumptions by the senior management; and - controls over the identification of impaired loans and advances, the data transfer from source systems to impairment models and model outputs to the general ledger and the calculation of the impairment allowance. <p>For loans which are individually assessed for impairment, we performed the following procedures on a sample basis:</p> <ul style="list-style-type: none"> - tested assumptions underlying impairment calculation including forecasted future cash flows, discount rates and estimated recovery from any underlying collateral etc; - tested loans and advances (including loans that had not been identified by management as potentially impaired) to form our own assessment as to whether impairment events had occurred and to assess whether impairment had been identified and recorded in a timely manner; and

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Report on the audit of the consolidated financial statements (continued)

Key audit matters (continued)

Key audit matter	How our audit addressed the key audit matter
<p><i>Impairment of loans and advances (continued)</i></p>	<ul style="list-style-type: none"> - tested loans and advances for economic sectors adversely affected by the current economic conditions to evaluate management's impairment assessment for such loans as per the Group's internal credit grading processes. <p>For corporate collective impairment models used by the Group, we tested on a sample basis:</p> <ul style="list-style-type: none"> - the extracts of historical data from underlying systems; - the assumptions used by management including probability of default; and - the calculations within the model. <p>For retail collective impairment, we assessed the reasonableness of the net flow rate model used by the Bank by performing the following:</p> <ul style="list-style-type: none"> - Assessed the appropriateness of the qualitative and quantitative changes in the underlying loan portfolio on a sample basis; - Tested the veracity of the data inputs used in the models including the flow of gross exposures, historical loss rates and analysis of delinquency bandings on a sample basis; and - Recalculated the model output calculations.

Independent auditors' report to the shareholders of The Saudi British Bank (A Saudi Joint Stock Company)

Report on the audit of the consolidated financial statements (continued)

Key audit matters (continued)

Key audit matter	How our audit addressed the key audit matter
<p><i>Valuation of derivatives</i></p> <p>The Group has entered into various derivatives including special commission rate and currency swaps ("Swaps"), spot and foreign exchange forward contracts ("Forwards"), special commission rate and currency options ("Options"). Certain derivative contracts are over the counter ("OTC") derivatives and hence, the valuation of these contracts is subjective as it takes into account a number of assumptions and model calibrations including adjustments to counterparty's own credit risk.</p> <p>The majority of these derivatives are held for trading. However, the Group utilizes certain Swaps for hedge accounting purposes for hedging fair value or cash flow risks. Valuation of derivatives could have a material impact on the consolidated financial statements.</p> <p>We considered this as a key audit matter as there is complexity and subjectivity involved in determining the valuation of derivatives, where complex modelling techniques are being used.</p> <p><i>Refer to the significant accounting policies note 2(d) to the consolidated financial statements and note 10 which explains the derivative positions and the valuation methodology used by the Group.</i></p>	<p>We assessed the design and implementation, and tested the operating effectiveness of the key controls over management's processes for valuation of derivatives including the testing of relevant automated controls covering the fair valuation process for derivatives.</p> <p>We selected a sample of derivatives and:</p> <ul style="list-style-type: none"> - Tested the accuracy of the particulars of derivatives by comparing the terms and conditions with relevant agreements and deal confirmations; - Evaluated and checked the methodologies, inputs and assumptions used by the Group in determining fair values; - Involved our valuation specialists to perform an independent valuation of the derivatives and compared the result with management's valuation; and - Considered the adequacy of the Group's disclosures about the valuation basis and inputs used in the fair value measurement.

Independent auditors' report to the shareholders of The Saudi British Bank (A Saudi Joint Stock Company)

Report on the audit of the consolidated financial statements (continued)

Key audit matters (continued)

Key audit matter	How our audit addressed the key audit matter
<p><i>Fee from banking services</i></p> <p>The Group charges loan transaction and service fee upfront to the borrowers on loans. All such fees are an integral part of generating an involvement with the resulting financial instrument and therefore all such fees should be considered for making an adjustment to effective yield and such adjustment should be recognised in accordance with IFRS.</p> <p>However, due to the large number of transactions with mostly insignificant fee amounts, assessment of amortisation of fee income based on effective yield is made by the management based on certain thresholds. For transactions below the threshold, management performs an assessment at year end to estimate what the cumulative and for the current period potential adjustment would have been, had the required amounts been amortised on a loan by loan basis, and adjust if the impact is considered material.</p> <p>We considered this as a key audit matter since use of management assumptions and thresholds could result in material over / under statement of Group's profitability.</p> <p><i>Refer to the significant accounting policies note 2(g) to the consolidated financial statements.</i></p>	<p>We performed the following procedures:</p> <ul style="list-style-type: none"> - We assessed the design and implementation and tested the operating effectiveness of the controls over the consistent application of management's assumptions and thresholds for recognition of fee income. - We evaluated the assumptions and thresholds used by management for assessing the effective yield of loans and amortising fee income accordingly. - We obtained management's assessment of the impact of the use of assumptions and thresholds and: <ul style="list-style-type: none"> - traced the historical and current year data used by management to the underlying accounting records on a sample basis; - checked the accuracy of the management's assessment including calculations and related assumptions on a sample basis; and - considered the impact of non-amortisation of fees on an effective yield basis with regard to the net income for the year and the net equity at the reporting date amongst other measures.

Independent auditors' report to the shareholders of The Saudi British Bank (A Saudi Joint Stock Company)

Report on the audit of the consolidated financial statements (continued)

Key audit matters (continued)

Key audit matter	How our audit addressed the key audit matter
<p><i>Valuation of available for sale investments</i></p> <p>Available for sale investments comprise a portfolio of debt and equity investments. These instruments are measured at fair value with the corresponding fair value change recognised in other comprehensive income. The fair value of majority of these financial instruments is determined through the application of valuation techniques, which often involve the exercise of judgment by management and the use of assumptions and estimates.</p> <p>Estimation uncertainty exists for those instruments not traded in an active market and where the internal modelling techniques use significant observable valuation inputs (i.e. level 2 valuation).</p> <p>The valuation of the Group's available for sale investments in level 2 is considered a key audit matter given the degree of complexity involved in valuing these financial instruments and significance of the judgment and estimates made by management.</p> <p><i>Refer note 1.1(f)(ii) to the consolidated financial statements which explains critical accounting judgments and estimates, note 2(i)(ii) which details significant accounting policies and note 35 which explains the investment valuation methodology used by the Group.</i></p>	<p>We assessed the design and implementation and tested the operating effectiveness of key controls over management's processes for performing valuation of investments classified as available for sale, which are not traded in an active market.</p> <p>We performed an assessment of the methodology and the appropriateness of valuation models and the inputs used to value available for sale investments.</p> <p>We tested the valuation of a sample of available for sale investments not traded in an active market. As part of these audit procedures we assessed the key inputs used in the valuation such as expected cash flows, risk free rates and credit spreads by benchmarking them with observable external data.</p>

Independent auditors' report to the shareholders of The Saudi British Bank (A Saudi Joint Stock Company)

Report on the audit of the consolidated financial statements (continued)

Key audit matters (continued)

Key audit matter	How our audit addressed the key audit matter
<p><i>Impairment of investments</i></p> <p>As at 31 December 2017, the Group held investments (net of impairment) of Saudi Riyals 26.977 billion. These investments comprise of equities, government and corporate bonds/sukuk, which are subject to the risk of impairment in value due to either adverse market conditions and/or liquidity constraints faced by the issuers.</p> <p>For assessing the impairment of equities, management monitors volatility of share prices and uses the criteria of significant or prolonged decline in their fair values below their costs as the basis for determining impairment. A significant or prolonged decline in fair value of an equity instrument below its cost represents objective evidence of impairment. The determination of what is significant or prolonged requires judgment. In assessing whether it is significant, the decline in fair value is evaluated against the original cost of the equity instrument. In assessing whether it is prolonged, the time-period for which the fair value of the equity instrument has been below its original cost is evaluated.</p> <p>For assessing the impairment of other instruments including debt instruments such as government and corporate bonds/sukuk, management considers them to be impaired when there is evidence of a deterioration in the financial health of the investee, economic sector performance, changes in technology and operational and financing cash flows.</p> <p>We considered this as a key audit matter since the assessment of impairment requires significant judgment by management and the potential impact of impairment could be material to the consolidated financial statements.</p> <p><i>Refer to note 2(m) of the consolidated financial statements for the accounting policy relating to the impairment of investments, note 1.1(f)(iii) for the critical accounting judgements and estimates, and notes 31 and 32 for the disclosures of credit and market risks respectively.</i></p>	<p>We assessed the design and implementation and tested the operating effectiveness of the key controls over management's processes for identification of indicators of impairment such as significant or prolonged decline in the fair value of equities below their original cost and/or any issuer defaults relating to other investments including government and corporate bonds/sukuk.</p> <p>For equity investments, on a sample basis, we:</p> <ul style="list-style-type: none"> - Assessed the appropriateness of management's criteria for determining the significant or prolonged decline in the value of investments; - Evaluated the basis for determining the fair value of investments; - Independently tested the valuations of investments; and - Considered the price fluctuation / movement during the holding period to determine if the significant or prolonged criteria is met. <p>For other investments including government and corporate bonds/sukuk, on a sample basis, we assessed the creditworthiness of counter parties based on available market information and assessed cash flows from the instruments, as provided by the management, to consider any defaults based on contractual terms and conditions of these instruments.</p>

Independent auditors' report to the shareholders of The Saudi British Bank (A Saudi Joint Stock Company)

Report on the audit of the consolidated financial statements (continued)

Key audit matters (continued)

Key audit matter	How our audit addressed the key audit matter
<p>Zakat</p> <p>The Group files its tax/zakat return with the General Authority of Zakat and Tax ("GAZT") on an annual basis. The GAZT has issued assessment orders for the years from 2005 up to 2009, which resulted in significant additional exposure amounting to Saudi Riyals 433 million. The significant additional exposure mainly relates to zakat and resulted due to disallowance of certain long-term investments and the addition of long term financing to the Zakat base by the GAZT. The interpretation of the GAZT is being challenged by the Bank and the appeal proceedings are underway at various levels of available appellate forums.</p> <p>Assessments for the years 2010 onwards are yet to be raised. However, in line with the assessments finalised by the GAZT for the years 2005 to 2009, if long-term investments are disallowed and long-term financing is added to the Zakat base this would result in significant additional zakat exposure. The amount of the potential additional zakat exposure is not disclosed in the consolidated financial statements as management expects that such disclosure might affect the Bank's position in this matter.</p> <p>The management makes judgments about the incidence and quantum of zakat liabilities (which are subject to the future outcome of assessments by the GAZT) and based on such judgments, management expects a favourable outcome of the appeal process.</p> <p>We considered this as a key audit matter as it involves significant management judgement and estimation and the additional exposure can be material to the consolidated financial statements.</p> <p><i>Refer to note 2(v) for the accounting policy relating to zakat and note 27 for the related disclosures for zakat.</i></p>	<p>In order to assess the status and likely outcome of the matter, we obtained correspondences between the Group, GAZT and Group's zakat consultants to determine the amount of the additional demand made by the GAZT. We further obtained the related appeal documents to confirm the fact that the matter has been contested at various appellate forums and to assess the status of those appeals.</p> <p>We held meetings with those charged with governance and senior management of the Group to obtain update on the zakat matter and the results of their interactions with the relevant appellate forums.</p> <p>We also used our internal specialists to assess the appropriateness of the exposure disclosed for the years assessed by GAZT, the appropriateness of management's judgments relating to the zakat matter in light of the facts and circumstances of the Bank and the appropriateness of the provision held by the Group.</p> <p>We also assessed the appropriateness of the disclosures included in the consolidated financial statements of the Group.</p>

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Report on the audit of the consolidated financial statements (continued)

Other information included in the Bank's 2017 Annual Report

The Board of Directors of the Bank (the "Directors") are responsible for the other information. The other information consists of the information included in the Bank's 2017 annual report, other than the consolidated financial statements and our auditors' report thereon. The annual report is expected to be made available to us after the date of this auditors' report.

Our opinion on the consolidated financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

When we read the other information, if we conclude that there is a material misstatement therein, we are required to communicate the matter to those charged with governance.

Responsibilities of the Directors and those charged with governance for the consolidated financial statements

The Directors are responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRSs as modified by SAMA for the accounting of zakat and income tax, the applicable requirements of Regulations for Companies, the Banking Control Law in the Kingdom of Saudi Arabia and the Bank's By-Laws, and for such internal control as the Directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the Directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Independent auditors' report to the shareholders of The Saudi British Bank (A Saudi Joint Stock Company)

Report on the audit of the consolidated financial statements (continued)

Auditors' responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with International Standards on Auditing as endorsed in the Kingdom of Saudi Arabia will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with International Standards on Auditing as endorsed in the Kingdom of Saudi Arabia, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Directors.
- Conclude on the appropriateness of the Directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Group to cease to continue as a going concern.

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Report on the audit of the consolidated financial statements (continued)

Auditors' responsibilities for the audit of the consolidated financial statements (continued)

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain jointly responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

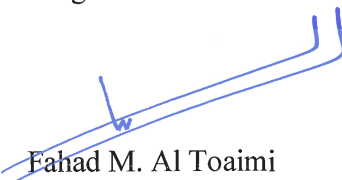
Independent auditors' report to the shareholders of The Saudi British Bank (A Saudi Joint Stock Company)

Report on other legal and regulatory requirements

Based on the information that has been made available to us, nothing has come to our attention that causes us to believe that the Bank is not in compliance, in all material aspects, with the applicable requirements of the Regulations for Companies, the Banking Control Law in the Kingdom of Saudi Arabia and the Bank's By-Laws in so far as they affect the preparation and presentation of the consolidated financial statements.

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